



BEFORE THE STATE BOARD OF EQUALIZATION  
OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of )  
F. SETH AND LEE J. BROWN )

Appearances:

For Appellants: F. Seth Brown, in pro. per.

For Respondent: Paul J. **Petrozzi**  
Counsel

## OP I N I ON

This appeal is made pursuant to section 18594 of the Revenue and Taxation Code from the action of the Franchise Tax Board on the protest of F. Seth and Lee J. Brown against proposed assessments of additional personal income tax in the amounts of **\$1,124.60, \$2,239.40** and \$887.04 for the years 1972, 1973 and 1974, respectively.

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The principal occupation of F. Seth Brown (hereafter referred to as appellant) is that of a bank executive. In addition to his salary from the bank, he received dividend and interest income- and income from several trusts and from sales of property. In 1972 appellant purchased a 37-foot fishing boat having about a 100-mile range with the asserted intention of engaging in commercial fishing off the southern California coast in the San Diego area. The commercial fishing for albacore and swordfish was done primarily on weekends. Appellant's son apparently was employed on a full-time share basis during the appropriate season. While others were sometimes employed on days when fishing prospects were positive, the crew usually consisted of appellant and his son. Admittedly, the boat was used for personal purposes about 30 percent of the time. Appellant has provided government data concerning the California albacore catch during the years in question. It appears that in those years the albacore catch reached a low point due to natural phenomena.

For each of the years in issue, appellant reported income and expenses from the fishing boat operation as follows:

<u>Year</u>	<u>Income</u>	<u>Expense</u>	<u>Loss from Fishing</u>
1972	\$1,694	\$13,404	\$11,710
1973	360	13,407	13,047
1974	- 943	<u>9,573</u>	<u>8,630</u>
Totals	\$2,997	\$36,384	\$33,387

Subsequent to 1974, appellant temporarily abandoned all efforts at commercial fishing. Respondent characterized the fishing operation during the years in question as a "hobby," rather than an activity engaged in for profit. Consequently, respondent disallowed the deduction of the claimed expenses to the extent they exceeded the limitations imposed by section 17233 of the Revenue and Taxation Code. Appellants appealed this action, claiming the expenses were fully deductible under sections 17202 and 17252 of the Revenue and Taxation Code.

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Section 17233 provides:

(a) In the case of an activity engaged in by an individual, if such activity is not engaged in for profit, no deduction attributable to such activity shall be allowed under this part except as provided in this section.

(b) In the case of an activity not engaged in for profit to which subdivision (a) applies, there shall be allowed--

(1) The deductions which would be allowable under this part for the taxable year without regard to whether or not such activity is engaged in for profit, and

(2) A deduction equal to the amount of the deductions which would be allowable under this part for the taxable year only if such activity were engaged in for profit, but only to the extent that the gross income derived from such activity for the taxable year exceeds the **deductions** allowable by reason of paragraph (1).

(c) For purposes of this section, the term "activity not engaged in for profit" means any activity other than one with respect to which deductions are allowable for the taxable year under Section 17202 or under subdivision (a) or (b) of Section 17252.

Accordingly, an activity is not engaged in for profit if deductions with respect to the activity are not allowable as trade or business expenses under section 17202, or as expenses incurred for the production or collection of income, or the management, conservation **or** maintenance of property held for the production of income under section 17252. Section 17202, 17233 and 17252 are substantially identical to sections 162, 183 and 212, respectively, of the Internal Revenue Code of 1954.

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Focusing on subsection (c) of section 17233, the disposition of this appeal turns on the question of whether appellants' acquisition and operation of the boat was an activity engaged in for profit. In order to prevail, appellants must establish that they acquired and held the boat primarily for profit-seeking purposes, and not primarily for personal recreational or other non-profit purposes. (Francis X. Benz, 63 T.C. 375 (1974); Joseph W. Johnson, Jr., 59 T.C. 791 (1973); Michael Lyon, ¶ 77,239 P-H Memo. T.C. 1977; Appeal of Clifford R. and Jean G. Barbee, Cal. St. Bd. of Equal., Dec. 15, 1976.) Whether property is held for the primary purpose of making a profit is a question of fact on which the taxpayer bears the burden of proof. (Appeal of Clifford R. and Jean G. Barbee, supra.) The absence of a **profit is not determinative**, but the activity must be of such a nature that the taxpayer had a good faith expectation of profit. (Carkhuff v. Commissioner, 425 F.2d 1400 (6th Cir. 1970); Joseph W. Johnson, Jr., supra.) Also, the taxpayer's expression of subjective intent is not controlling. Rather, the taxpayer's motives must be determined from all the relevant **facts** and circumstances. (Joseph W. Johnson, Jr., supra; Appeal of Clifford R. and Jean G. Barbee, supra.)

One of the relevant factors to be considered is the manner in which appellant conducted the fishing operation. Generally, the commercial fishing was only done on weekends. This was in sharp contrast to the approach taken by the typical profit-seeking commercial fishing enterprise where fishing was done virtually full-time. It seems clear that under appellant's mode of operation there was virtually no chance of realizing a profit. Appellant's lack of concern for earning a profit is illustrated by the fact that even after incurring expenses approximately eight times greater than revenues during the first year of operation, no substantial change was made. Instead, appellant persisted in his unprofitable "weekends only" approach, and in the second year incurred expenses approximately 37 times greater than revenues. Again appellant failed to change his approach and he continued to operate at a loss during the third and final year of the venture.

We are also impressed by the fact that appellant's principal occupation, as a bank executive, limited the amount of time he could devote to fishing. In addition, his boat had a limited range. Thus when

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the albacore catch fell off he did not have the ability to travel farther in order to improve the chances of a better catch, nor did he have the time available to spend more days fishing. The credibility of appellant's asserted profit motive is further diminished upon consideration of his financial status and the fact that the losses in question, if deductible, would provide considerable tax advantages. Indeed, appellant's combined income placed him in a tax bracket high enough so that qualifying losses from a sideline activity could generate substantial tax savings. An arrangement to minimize tax liability is no substitute for the bona fide expectation of profit required for deduction of losses such as those incurred by appellant.

At the hearing of this matter, it became clear that appellant could probably have made more money by simply conducting charter sportfishing excursions on weekends. Appellant's failure to make this or any other adjustment in the operation of his boat, in light of the great disparity between expenses and the **revenue realized** from the commercial fishing venture, causes us to doubt the sincerity of his asserted expectation of earning a profit on the entire operation. (Francis X. Benz, supra; Margit Sigray Bessenyei, 45 T.C. 261 (1965).)

Based upon the record before us, we conclude that appellants have failed to carry their burden of proving that the fishing activity was engaged in for profit. Therefore, the deduction of the expenses related to the boat is subject to the limitations imposed by section 17233 and, accordingly, respondent's action in this matter must be sustained.

Q R D E R

Pursuant to the views expressed in the opinion of the board on file in this proceeding, and good cause appearing therefor,

IT IS HEREBY ORDERED, ADJUDGED AND DECREED, pursuant to section 18595 of the Revenue and Taxation Code, that the action of the Franchise Tax Board on the protest of F. Seth and Lee J. Brown against proposed assessments of additional personal income tax in the amounts of \$1,124.60, \$2,239.40 and \$887.04 for the years 1972, 1973 and 1974, respectively, be and the same is hereby sustained.

William W. Davis Chairman

John J. Edgar, Member

John Kelly, Member

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